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ABSTRACT

Instead of adopting an entirely new school finance system to replace an inequitable system threatened by lawsuits, the Arkansas legislature has chosen to repair Act 34 of 1983. Two major changes enacted in 1993 (recalculation of state aid for districts experiencing growth and a change in a district's real property charges when calculating state aid) seem doomed to failure. The major reason why Act 34 does not equalize may be its use of artificial numbers to calculate local wealth. Rather than abandon these fictional figures, the legislature seems determined to juggle them. Because the millage charge on real property adopted in 1983 was much too low, the cap was eventually raised to match the state average millage figure. Even so, the difference between the current charge and the average millage is some 4.84 mills, requiring an increase of $152.5 million to equalize them. Also, outdated numbers for personal and utility property have been used to calculate current wealth. A short-range effort to stop penalizing districts for growth produced a confusing funding formula that penalizes stable or declining districts. These and other factors add up to increasing inequity for students and taxpayers. It is hoped that the new finance commission will design a better system. (MLH)

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ARKANSAS' SLIDE FROM EQUITY

Presented by

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to

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Arkansas is currently trapped on the horns of a dilemma. It can adopt an entirely new system of school finance to replace the present one under which suits are being threatened or it can attempt to repair the current system to try to have it accomplish some form of equity. Currently, the latter scenario seems to be the one taken.

The present finance system based on Act 34 of 1983 does not attain equity. Several studies have shown that according to any measure of equity, there is less today than in 1983 before the law was passed. Thus, the idea of a second equity lawsuit is being seriously pursued. The original suit cannot be reopened as the trial judge retained jurisdiction and then died.

The legislature, rather than opting for a new plan even in the face of legal threats, decided to attempt to repair Act 34. It made several major changes in the law in the 1993 session. The two most important were the recalculation of the state aid for districts experiencing growth and a change in the charge which is made against the real property of a school district in the calculation of state aid. Essentially these are both long range and short range attempts at equity. However, they seem doomed to failure.

Perhaps the major reason why Act 34 does not equalize is the fact that it has used so many artificial numbers rather than real ones on its calculation of local wealth. The legislature has seemed to have an inkling of this but rather than abandon the fictional figures it has determined to jiggle them.

The Long Range Solution

When Act 34 was passed in 1983, real property was charged at the rate of 19 mills, regardless of the actual millage of the district. This was to be the standard levy to calculate all real property in the state. It became evident by 1989 that this rate was much too low. Therefore, the limit on millage was allowed to rise to 25 mills. It was to float there. An increase in the charge of .1 mills was to be caused by an increase of 2.5 million dollars from the state in Minimum Foundation Program aid. As a result, by 1993, the charge rose to 24.2 mills. However, since the average millage in the state was 29.04, it was apparent that the cap was still set too low.

In 1993, the cap was raised to whatever figure that the state average millage reached. It would continue to increase on the basis of .1 mills for every new appropriation of 2.5 million dollars. It is

hoped that such a move will result in more equity. However, the difference between the current charge and the current average millage is some 4.84 mills. This would mean an increase in state appropriation of 152.5 million dollars to equalize them. The total Minimum Foundation Aid in 1992-93 was 872 million. Thus, to equalize the current charge and the current average millage would require a 17 percent increase in state aid.

Even when this takes place, approximately one-half of the schools will be taxing locally below these figures, thus not delivering the equalized amount to their pupils and roughly one-half of the districts will be taxing at a higher rate guaranteeing their students more funds. Hence, inequity will continue.

To further confuse this point, the state average millage rises at a rate of better than one-half a mill per year. Between 1991-92 and 1992-93 it was .66 mills. Hence, just to stay even, that is 4.84 mills behind the average, the state will have to raise its appropriation at the rate of 17.5 million per year or 35 million in a biennium, the period for which state budgets are made.

It is difficult to imagine the increases being made under current conditions of the states

economy. Thus, the state will be in a similar situation to a dog chasing its tail.

Archaic Numbers

Until March of this year one of the major features of the law was the use of outdated numbers in the calculation of current wealth. This was done for two types of property which had been created by Amendment 59, namely personal property and carrier and utility property.

The law set as a base year for these, the year prior to real property reassessment. Any increase or decrease in current yield over the amount collected thus was translated into a percentage rise or drop. That percentage difference was then added or subtracted from the pre real property reassessment assessment and 45 mills charged against it. To say this was confusion is something of an understatement.

The actual wording of the statute is almost as obtuse. It reads in part for both personal and carrier and utility property, that:

> For school districts located in counties that have been reassessed, the charged assessment used shall be the actual assessment for the calendar year prior to the base year multiplied by the ratio of the taxes due to be collected in

the current year to the taxes due to be collected in the base year.

Exactly what this means has become a bone of contention. The State Department of Education, using as its rationale legislative intent, decided to calculate increased taxes is personal and utility and carrier property as that which occurred only on the bases of increased assessment not millage increases. It was thought that the legislature had not intended to penalize a school district for having raised its local millage.

This practice has been common since about 1989, not 1993 as the media has reported because it was only then that districts began to equalize their real and personal property millages. Personal and carrier and utility yields having been frozen until that event took place.

Earlier this year, a state representative discovered this practice and went to the governor to complain. He wanted a literal interpretation of the law to be followed. The governor agreed. The media was full of stories as to how poorer districts would receive more money and wealthier ones less. In fact, a literal interpretation of the law hurts high effort districts while rewarding less effort ones. This is irrational.

Thus, there was considerable support for a Special Session of the Legislature to correct the problem. The Special Session of the legislature met on February 28, 1994. It lasted but three days.

When all of the oratory ceased, it did three things:

1. It appropriated 3.7 million dollars to cover any losses which school districts might suffer during the rest of the current fiscal year due to changes in Act 34.

2. It passed Act 1007 which, starting currently gets rid of all the historical numbers. There will be only one kind of property. It will be charged at the rate of 25 mills.

3. It appropriated 2.83 million dollars to cover the losses that will be suffered by 21 school districts due to the abandonment of the old system. They will receive 85% of their loss the first year of the charge, 59% percent the second, and 25% the third.

One final detail. The state set up a finance commission to study Act 34. The major drawback to the group selected is that they are all members of the legislature and state board of education. It seems a good group to achieve more political deals and less equity.

The Short Range Solution

Equity in the short run was addressed by an attempt to stop penalizing districts for growth. It is a common feature of state aid programs that the money due a district is based on the enrollment in the preceding year. This means that if a district is growing rapidly, its local resources are stretched, often too far, to deliver a quality education.

The new adjustment is the result of a rather confusing formula in which the ratio of the first quarter ADM for the previous year to the three quarter average ADM is compared to the current ADM and a projected three quarter average. In this case, if where growth can be demonstrated in this fashion, the state aid for such a district is to be recalculated and paid by the end of the third quarter of the school year. At least that was what the legislature thought it was doing. But, it runs full tilt into the long range solutions.

Some 18 million dollars was withheld from distribution to the Minimum Foundation Program in the summer of 1993 to cover the needs of the growing districts. The trouble arises from the fact that adding 18 million dollars increases the charge in real property by some .7 mills. The charge will be raised from the current 24.2 mills to 24.9. This will require a recalculation of all districts state aid both

those which have not experienced growth and those which have. The former could well lose state aid.

The State Department of Education, basing its logic on legislative intent, claimed that the charge should be held at 24.2 thus assuring all districts that such a move would prevent a loss of funds. However, a group districts threatened a lawsuit based upon the clear statement in the other part of the law that the charge would increase if state aid were increased. This now seems to be the case. The charge will rise. All districts will be recalculated and funds for some will be cut. Therefore, rather than the local resources of growing districts being stained, the local resources of stable or declining districts will be strained instead. Recalculation will not solve the problem. Rather it will shift its incidence.

Further Cuts in the Tax Base

To prove to the recalculated districts that they would not be the only ones whose local resources were strained, the legislature and the courts managed to cut local assessment.

The legislature did so by changing the method by which automobiles held by dealers were assessed. Until now, automobile dealers were assessed a property tax based upon their average

inventory for a year. No longer. The legislature changed this to the value of the cars on the lot on a given day. Guess how full the lots will be on that day!

One of my acquaintances is a tax assessor in Texas. They had a similar law to our new one. They found it profitable to rent an aircraft and go out and photograph the cars stored in fields in rural areas to avoid the tax. Arkansas assessors might well have to adopt similar tactics.

No one is estimating the loss to schools if the assessment changes. It will be large and it will be real!

The courts were not to be outdone with generosity with school funds. On April 5, 1993, the State Supreme Court ruled that goods shipped out of Arkansas were not subject to a property tax. This line of reasoning will cost schools three million dollars but it made manufacturers happy. They will now have more funds with which to complain about the low quality of high school graduates in Arkansas.

As the tax base decreases, local funds can only be restored by millage increases on the remainder of the base. Thus, it is predictable that the state average millage will continue to rise in fairly large amounts. Therefore, an equalization model which depends on reaching the average

millage will have a more difficult time in doing so. The added state money required for such an event may well become more than anyone had thought and may be less easily raised.

Other Factors

There are three other disequalizing factors which were ignored by Act 34 as well and any successive legislation. There are Transportation Aid cuts, the 40 percent pullback, and the commission system for paying county employees.

Transportation Aid

For the past several years, the legislature has not fully funded transportation aid. This means that school districts must take money from the instructional program to spend on buses. The effect of this situation varies. Since the rather confusing three tiered formula for transportation aid is not particularly equalizing, some districts must deduct more than others from children's education.

The only attempt to alter this condition was the passage of a law allowing bonds to be sold to pay for buses. However, the bonds must be repaid and interest payments made. If transportation aid will not cover these then the funds must still be deducted from instruction.

The 40 Percent Pullback

An oddity of Arkansas school is what termed the "40 percent pullback." The Constitution of Arkansas forbids deficit funding. Therefore, schools engage in it regularly. This condition is caused by the fact that the school fiscal year runs from July 1 to June 30. The tax year on the other hand runs to October 14. Thus, the two are not synchronized.

It was determined some years ago, that 40 percent of the years taxes were paid prior to June 30. Therefore, when a school district constructs its budget, it subtracts 40 percent of the current year taxes and adds 40 percent of the estimated tax yield of the following year. This practice can cause severe dislocation. As just one example one district two years ago discovered that its largest tax payer, a nationally traded real estate development had declared bankruptcy. Had not a special appropriation been made for them, one-half of the teaching staff would have had to be riffed. Due to much fluctuation in tax collections which will not affect state aid until the following year, the pullback can act as a disequalizer.

The Commission System

It would seem that back in the Nineteenth Century, when the Arkansas Constitution was written, that there was a belief that paying county treasurers, assessors, and collectors on a commission basis would make them more efficient in their duties. It was to be a motivator to assure that they did not slacken their energies in the carrying out of their responsibilities.

However as the Twenty-First Century dawns, it seems evident that the commission system has an entirely different set of effects from those foreseen a century or so ago. What it does new is take money from children's education.

Only the treasurers percentage is set by law. The assessor and collector receive whatever sized commission check the County Quorum Court will approve. In the last study made of this practice, commissions ran from 7.5 to 14 percent of local school revenue with the average at 12.5. Therefore, when the state calculates all of the local school tax collection as being devoted to schools it maintains an irrational position if in fact a varying percentage is actually being distributed.

The Present Situation

All of these factors add up to increasing inequity both for the students and the tax payers. The difference between the highest and lowest expenditures per ADA is $3,964. This is more than the average expenditure per pupil. The difference between the highest and the lowest teacher salary is $14,994. This is almost as much as many districts pay beginning teachers. The state average as noted previously is 29.04. It is hard to believe that just 11 years ago, Arkansas received a court order requiring equity.

Each year the difference increases. Equity becomes less likely.

Conclusion

Thus, Arkansas seeks to move toward equity. Yet, its legislature and courts seem to be on an opposite track. On one hand, local tax receipts are cut, on another, the rates are forced upward. The real chance of attaining equity with these changes in the finance law seem dim indeed. Arkansas must try the other horn of the dilemma. It must design a new system of paying for the public schools. Hopefully, the new finance commission, regardless of its highly political overtones will design a better system.